ESO 1900

1992
Agricultural Outlook Overview

National Economy
Agricultural Policy
Farm Income and Finance

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National Economy

The national and international economies give agriculture some reason for optimism. Inflation, interest, and exchange rates are favorable. Reserve stocks and excess production capacity are down. The Soviets need food help and the world and U.S. economies are coming out of recession. These factors won't produce huge farm price rises in 1992 if harvests are plentiful. But any sign of a poor harvest in 1992 will send commodity prices soaring.

Slide: Economic Growth: Real GNP

The economy has been gradually slowing since 1987. It turned around by the end of the second quarter of 1991 but signs of growth are hard to find. The Blue Chip private forecast, a consensus from a number of economists, projects a 2.9% rate of growth for next year. The forecast in the figure of a similar rate in the last two quarters of 1991 is too optimistic. The economy grew only 2.4% (annual rate) in the third quarter of 1991. The economy is expected to move along more briskly and the forecast 2.9% growth rate in 1992 is feasible. That is far below the average growth of nearly 8% on an annual basis recorded in the quarters immediately following the previous eight recessions.

Slide: Consumer Price Index

Ordinarily a massive tax cut or increase in federal spending would quickly bring the economy out of recession. But huge federal deficits and accumulated debt of the last 8 years under economic recovery have removed fiscal policy as a major tool to jump start the economy. A tax cut or fiscal spending stimulus would be ill advised because the timing would be too late and would only add to a budget deficit already out of control. That places a major burden on monetary policy. Fortunately, the inflation rate is fairly low. The consumer price index increased at less than a 4% annual rate in the first three quarters of 1991 and inflation is expected to continue to be low.

Slide: Interest Rates

Low inflation not only means good news for prices paid by farmers but also it means that the government can increase the money supply and reduce interest rates to stimulate the economy. That stimulation is apparent in the falling interest rate on three-month Treasury bills. Interest rates on long-term bonds have held up because the public anticipates that inflation will continue in the future. Continued stimulation of the economy through lower interest rates is good news for farmers because interest is one of the largest items in the farm budget. But too much monetary expansion now could revive inflation because the effect could be felt in 6-12 months -- when the economy is progressing better and bottlenecks in supply could drive up prices.

Slide: Exchange Rates

Exchange rates have fallen sharply since 1985 but have somewhat leveled since 1987. Exchange rates made a considerable jump in early 1991 but can be expected to remain low in the future because confidence in the dollar is not great and because a low exchange rate will be necessary to allow American exports to compete in international markets. This in turn is necessary for export earnings to generate foreign exchange paying our huge international debt service obligations.

Slide: Top Six Markets Take 70% of U.S. Exports

A major impact of recession on agriculture comes through international linkages. Of particular concern is what is happening to the economies of the major markets for U.S. farm exports. Of critical importance is what happens in Japan, the European Community, and the Soviet Union.

Slide: Economic Growth Rates

Economic growth is expected to slow in Japan and Germany in 1992 but is expected to pick up in the European Community, including the U.K., and Canada. Overall world economic growth will pick up in 1992. That's favorable news for American farm exports but is somewhat offset by the lack of buying power in the Soviet Union and favorable crops in other countries such as Canada which compete with our farm exports.

Slide: Federal Budget Deficit

The federal budget deficit and GATT negotiations pose big unknowns for farm policy. The federal budget remains out of control but there is much talk of increasing the deficit through tax cuts or increasing spending for unemployment insurance payments or other social programs. If the economy recovers rapidly, Congress and the President could again seek a new accord to diminish red ink of the federal government.

Slide: Real U.S. CCC Net Outlays

Agriculture is vulnerable to federal budget cuts as apparent in the last budget accord. However, government costs of farm programs have diminished sharply since 1986 in absolute terms, as a proportion of GNP, and as a proportion of farm income. Hence any tampering to reduce the cost of farm programs to save federal outlays in 1992 is unlikely.

Another big sleeper is GATT negotiations. An agreement could call for reductions in farm price supports of up to 25% spread over several years. However, such cuts are unlikely to go into effect in 1992.

Farm Policy

Slide: Farm Policy Issues

Five farm policy issues in addition to those listed earlier impacting agriculture in 1992 include

1. Wetlands redefined.
2. Food safety.
3. Most favored nation status.
4. Canadian GRIP.
5. EC.

Slide: Wetlands Redefined

Farmers appear to be winning a battle to make the definition of wetlands less restrictive. President Bush has proposed that wetlands be redefined. Under the new definition wetlands would be defined as

(a) Land saturated with water 21 days during the growing season or continuously inundated by water for 15 days during the growing season.

(b) Hydric soils (muck, peat, etc.).

(c) Hydrophytic plants (cattails, water lilies, etc.).

To qualify as wetlands, soils would need to be all three of these. Under the old definition only one of (a), (b), or (c) had to apply. And for (a), there needed to be standing water or saturated soil within 18 inches of the surface only 7 days each year.

Slide: Food Safety

Congress members Bruce (IL) and Bliley (VA) have proposed a bill that would allow pesticides posing only a "negligible risk" to the public. This is less restrictive than the Kennedy (MA)/Waxman (CA) bill that would attempt to outlaw pesticides posing any risk. Virtually any pesticide poses some risk, however small. Recent EPA and other studies indicate that chemical risks in agriculture are less than was initially thought.

Slide: Most Favored Nation

It appears likely that the Soviet Union will receive Most Favored Nation status which entitles it to the low tariffs on their exports to the United States. Tariffs reduced to an average of about 5% will not do the Soviet Union much good in the short run because it has little to sell.

At the same time there is risk that Most Favored Nation status will be removed from China. That could mean serious disruption in trade including agricultural exports to both China and Hong Kong. There is probably a less than a 50-50 chance of MFN removed from China, however.

Slide: Canadian GRIP

GRIP stands for Gross Revenue Insurance Plan in Canada. It is patterned after the old Western grain insurance scheme in Canada but contains a number of new features. It is much more generous to producers and supports prices at approximately 50% over market levels of 1991. The cost is jointly paid by producers, provinces, and the national government. Because it does not call for production controls (although it does set some limits on how much production can be increased over previous levels), it poses some threat to U.S. farm exports. It is not a favorable development for U.S. farmers.

Slide: EC

There are hopeful signs of liberalization of the Common Agricultural Policy (CAP) of the European Community (EC). The EC has accumulated substantial reserves which will be given to the Soviet Union to ease the winter 1991-92 food shortage.

The EC has given encouraging but somewhat mixed signals that direct payments, tariffs, and production controls would replace the current CAP.

In another major development, the European Community has indicated that it will extend free trade advantages to the European Free Trade Association (EFTA) which includes the Nordic countries of Iceland, Norway, Denmark, and Sweden, as well as to Austria and Switzerland. That is not an unfavorable development for U.S. agriculture because the EFTA countries have supported agriculture at even higher rates than the

European Community. Hence production might actually be restrained somewhat in the EFTA countries.

Farm Income and Finance

Ohio agriculture has experienced one of the worst possible scenarios: A drought that is not widely shared and hence does not sharply drive up farm commodity prices. In addition Ohio farm income has been hurt because Ohio producers are specialized more in crops than are producers in many other states and farm prices in recent years have favored livestock more than crops. Relative profitability may change next year as crop prices are expected to rise more than livestock prices.

Slide: Real U.S. Farm Income and Components

Real U.S. crop receipts have diminished since 1981. Livestock receipts over the period since 1981 have held rather steady. Government payments and other income dropped significantly in the early 1980s but have held up rather well since. Total gross farm income has slacked off from the high levels of the 1989-90 years.

Slide: Real U.S. Farm Expenses and Components

Total production expenses have remained almost stable in real terms since 1986. That stability masks the fact that interest expenses and manufactured input (fuel, fertilizer, etc.) expenses have fallen while farm origin input, pesticide, repair and maintenance, and hired labor expenses have risen. Feed expenses have risen significantly since 1985 and are expected to rise again in 1992.

Slide: Real U.S. Farm Income and Expenses

Real gross farm income fell significantly more than real total expenses so that net farm income fell in 1991 as predicted in the outlook meetings last year.

Slide: Expected Change in 1992 Over 1991

In summary, U.S. crop receipts are expected to increase $2 billion in 1992 over 1991. The drop in hog and egg receipts is expected to be offset by an increase in beef, broiler, and turkey receipts and no change in dairy receipts to leave livestock receipts nearly unchanged in 1992. Mostly because of inflation and higher feed costs, production expenses are expected to rise $2 billion in 1992. This offsets the expected increase in gross farm income so that net farm income is expected remain almost unchanged in current dollars. However in constant or real dollars, net farm income is expected to be down somewhat.

Slide: Real U.S. Farm Assets, Debt, and Net Worth

Real farm assets declined sharply in the first half of the 1980s but have remained steady since. Meanwhile, farm debt continued to drop so that farm net worth has increased. The greater net worth has made farmers less vulnerable to economic setbacks. However, the drought has been especially hard on many financially vulnerable Ohio farmers. That partly explains why Ohio farm numbers declined more than usual in 1991.

Slide: Real U.S. Farm Financial Ratios

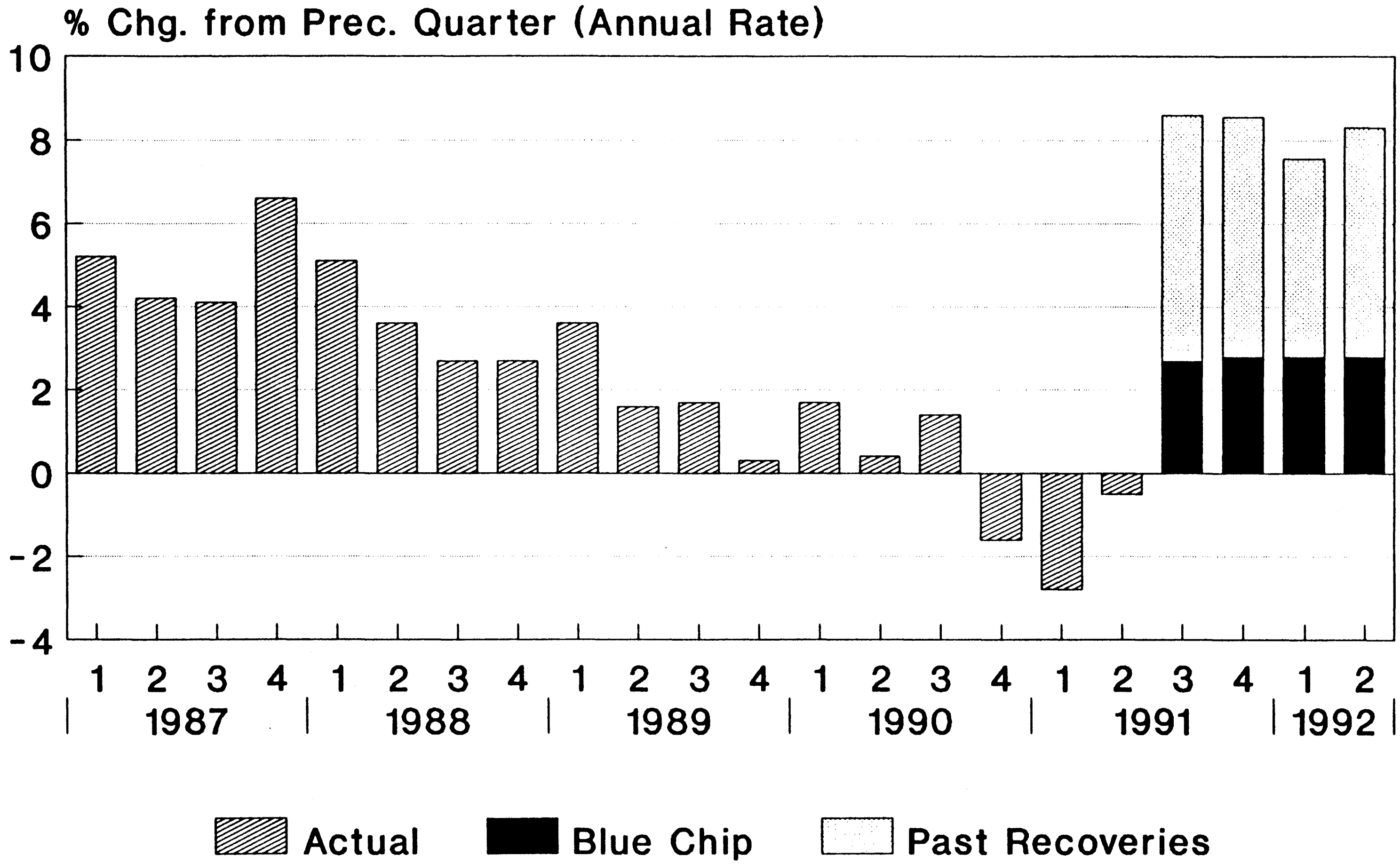
Debt-to-asset and debt-to-net farm income ratios indicate greater financial security and less vulnerability to risk by farmers.

Slide: Measures of Ohio Farm Household Financial Condition

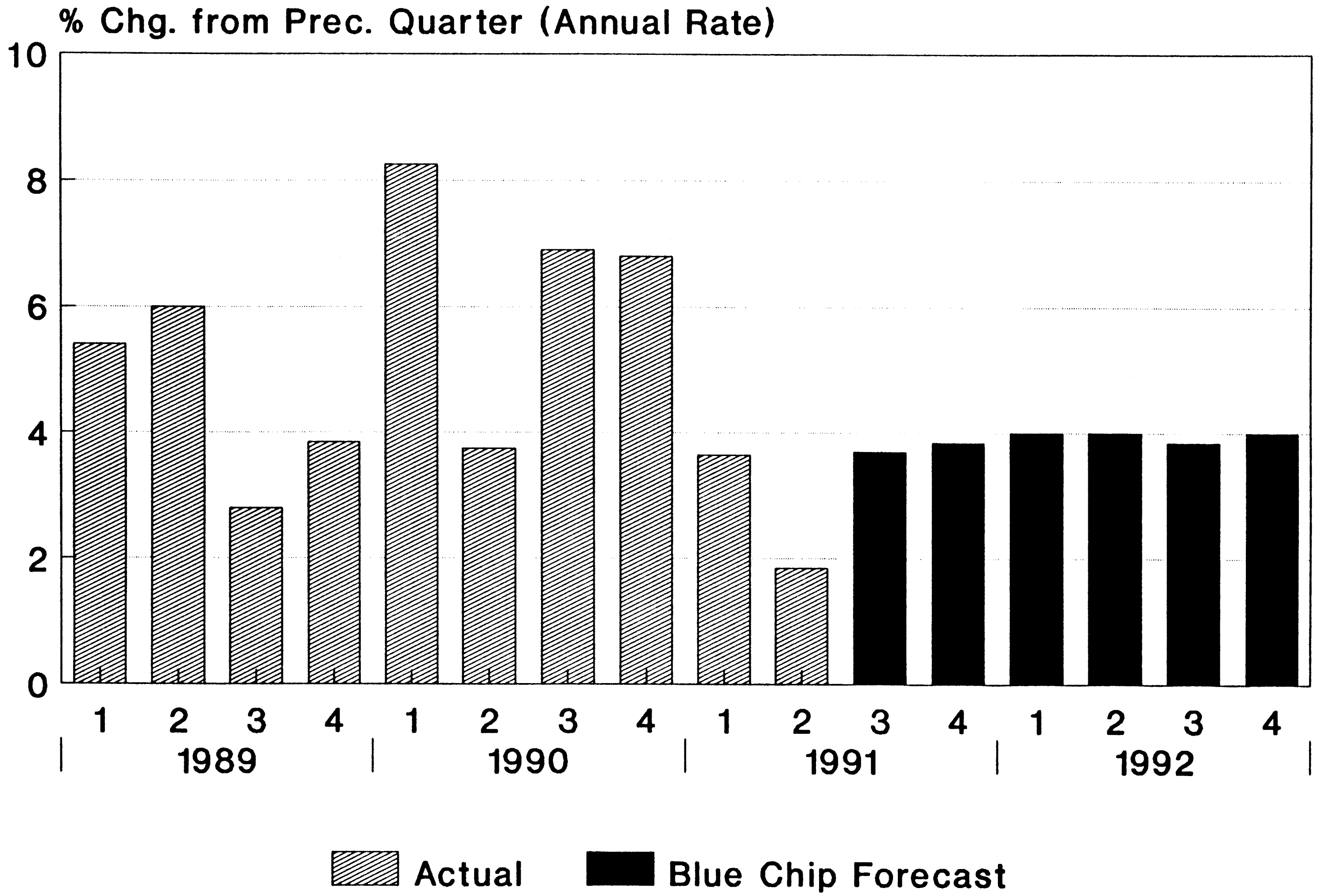
Ohio in many ways is a small-scale version of the national economy. The big difference in 1991 is the drought hit Ohio harder than it did other states. That has meant extreme economic hardship to many in agriculture. The situation would have been worse, however, if farm equity and debt-asset ratios had not recovered somewhat from mid-1980s conditions. In general, Ohio farmers have tended to have slightly lower debt-asset ratios than U.S. farmers. The degree of financial stress brought on by the drought and narrow profit margins in general depends heavily on a number of factors including farm size. In general, commercial farmers are more leveraged than other farmers. Hence as of late 1990, 3% of commercial farmers (with sales over $100,000) were financially vulnerable as measured by debt-asset ratios over 70%. Only 1% of small farms faced such financial vulnerability. Small farms had substantial off-farm income to cushion economic setbacks. In many cases, it was the mid-size farms which had less off-farm income than small farms but had higher production costs per unit than large farms. Thus many mid-size farms experienced severe financial stress in 1991.

In short, with normal weather 1992 promises to be a good but not great year. However, if there is a short crop (and some experts are predicting it), crop farmers would receive much higher prices.

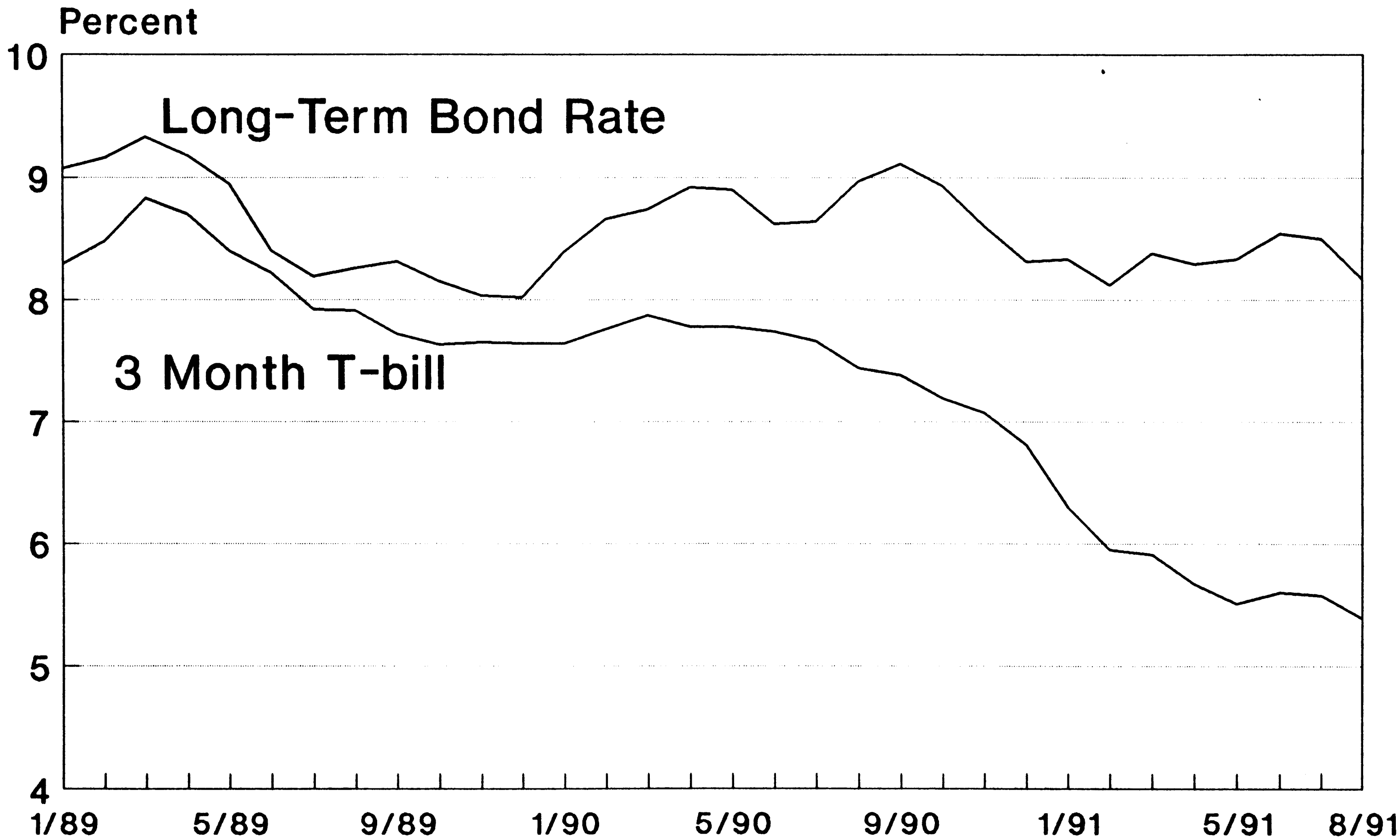
ECONOMIC GROWTH
Real GNP



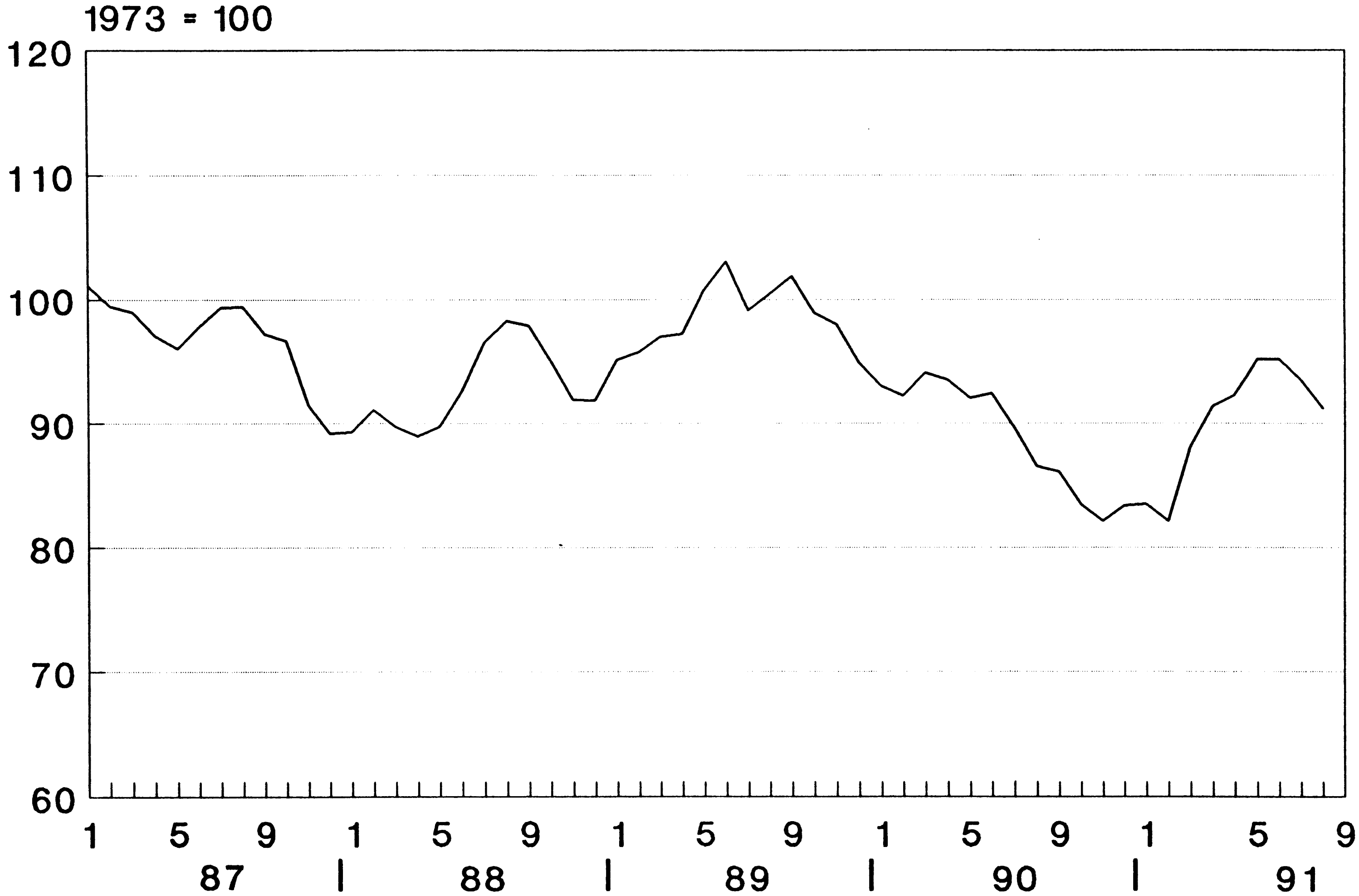
CONSUMER PRICE INDEX



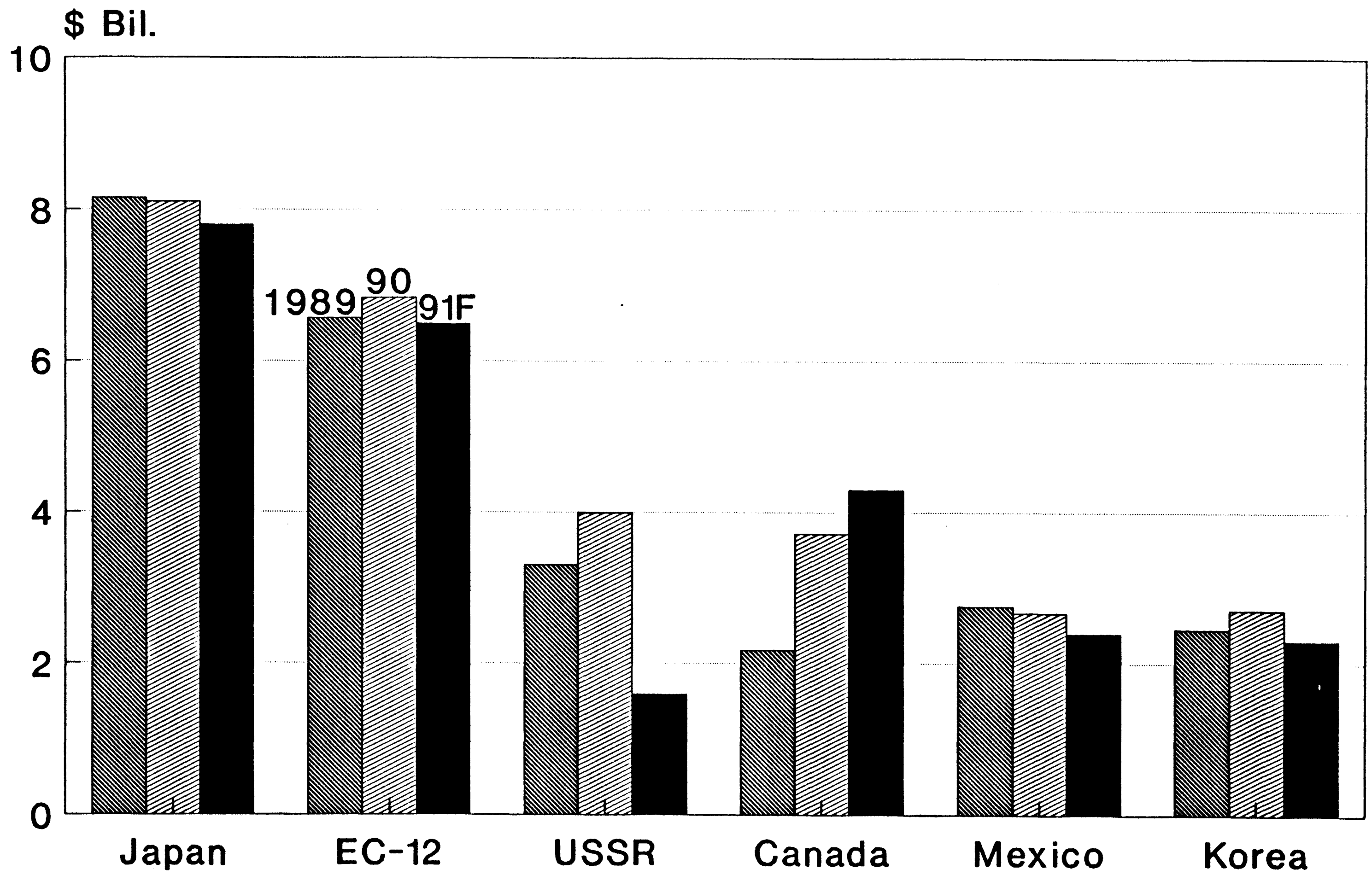
INTEREST RATES
U.S. Government Securities



EXCHANGE RATES
Trade-Weighted Valued of the Dollar



TOP SIX MARKETS TAKE 70% OF U.S. EXPORTS

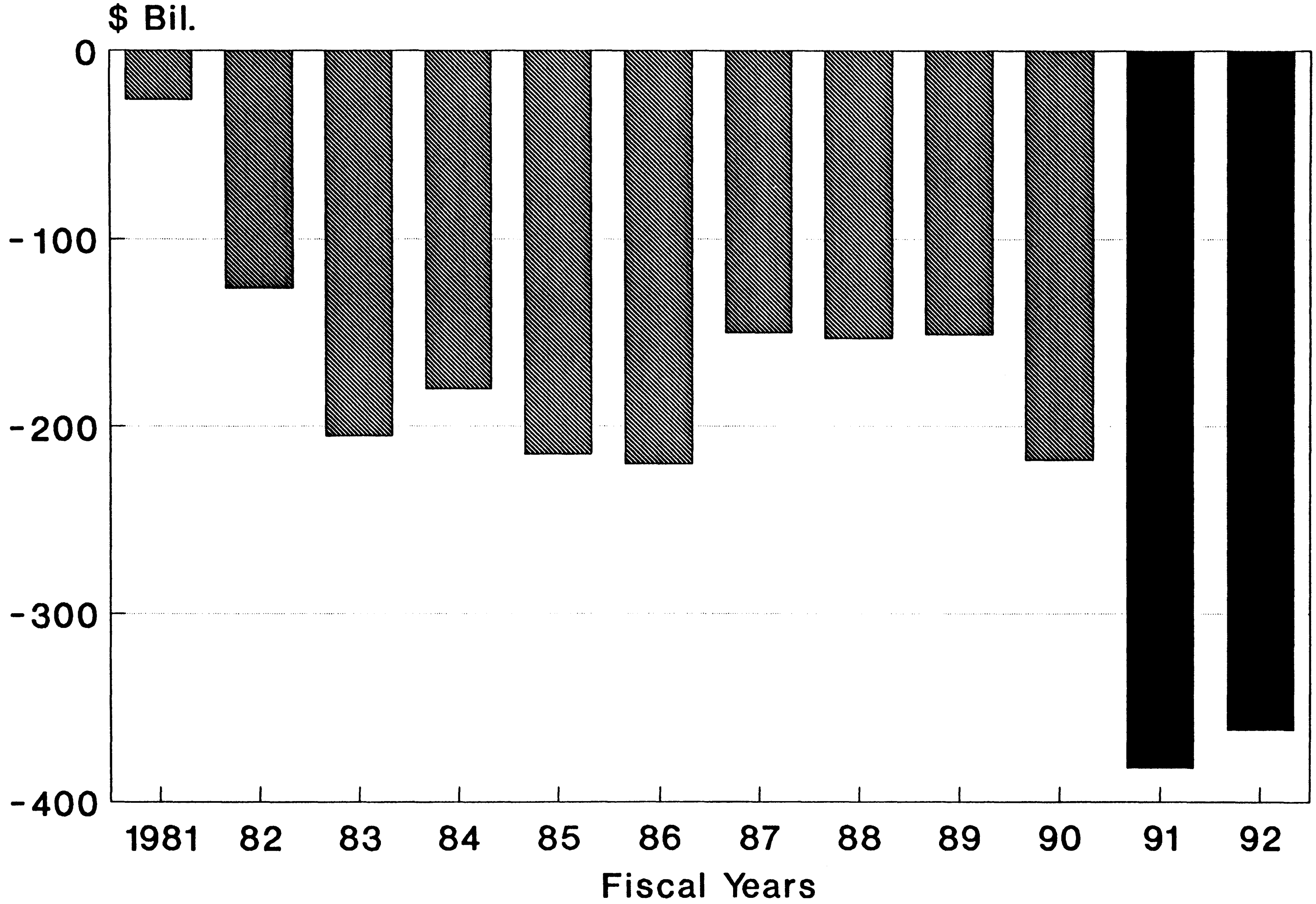


ECONOMIC GROWTH RATES

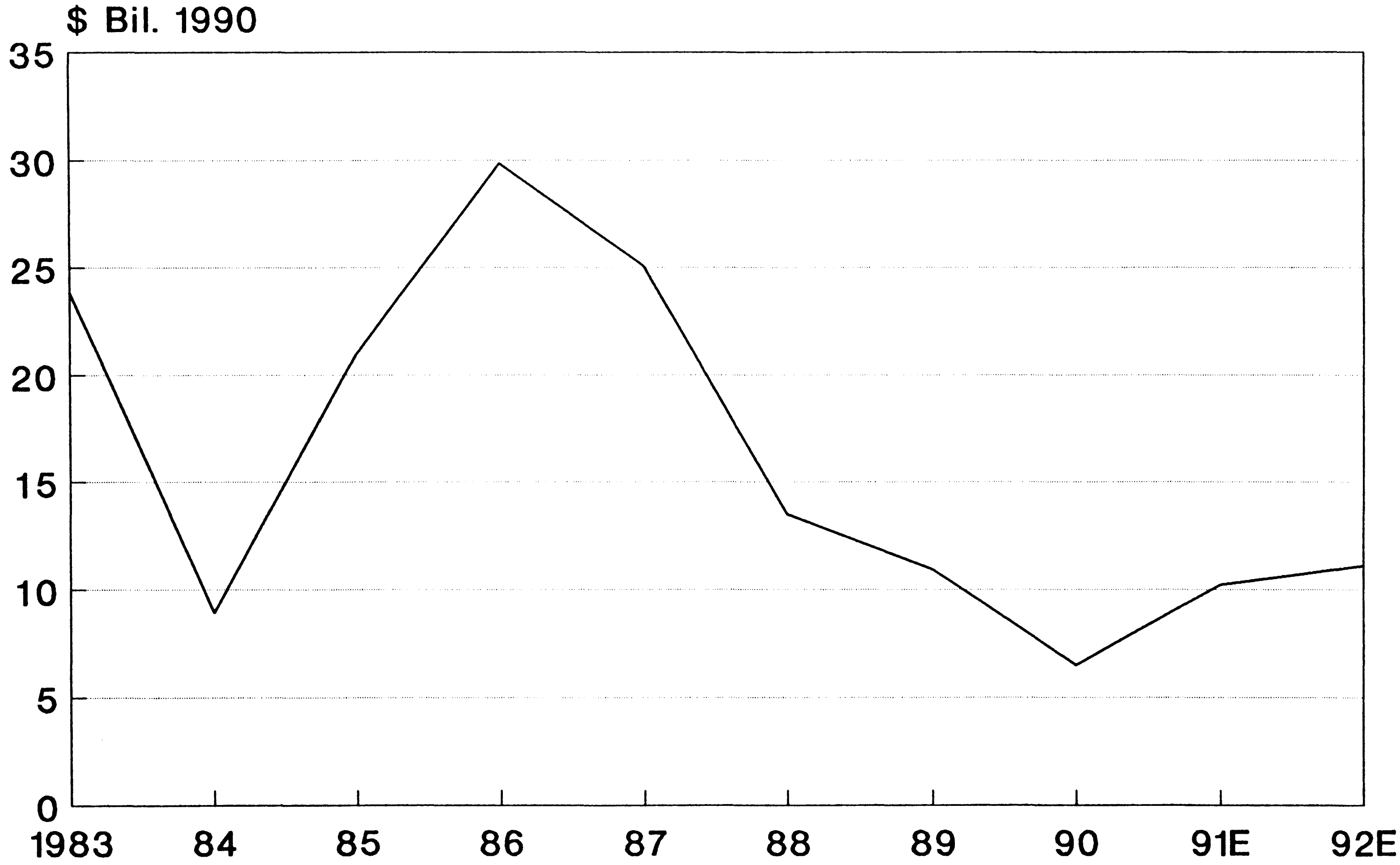
	1991	1992F
Japan	3.9	3.5[ab]
Germany	2.7	2.2[a]
U.K.	−1.5	2.1[a]
EC-12	1.7	2.9[b]
Canada	−1.2	3.3[ab]
World Less U.S.	1.4	3.3[b]
U.S.	−0.3	2.9

[a] The Economist, July 27, 1991.
[b] IMF.

FEDERAL BUDGET DEFICIT



REAL U.S.
CCC NET OUTLAYS



FARM POLICY ISSUES

1. Wetlands redefined.
2. Food safety.
3. Most favored nation.
4. Canadian GRIP.
5. EC.

WETLANDS REDEFINED

* Old: (a) Standing water or saturated within 18 inches of surface 7 days each year or
  (b) Hydric soils (muck, peat, etc.) or
  (c) Hydrophytic plants (cattails, etc.).

* New: (a) 21 days of saturation to surface or 15 days of continuous inundation in growing season (Bush proposal).
  All three of new (a), (b), and (c).
  All agencies have same rules.

FOOD SAFETY

* Bruce/Bliley Bill:
  Would allow pesticides that posed only a "negligible risk" to public.

* Kennedy/Waxman Bill:
  More restrictive.

MOST FAVORED NATION

* Give to USSR?

* Remove from China?

CANADIAN GRIP

* Gross Revenue Insurance Plan.

* No production control.

* Paid by producers, provinces, and national government.

* Support 50% over market.

EC

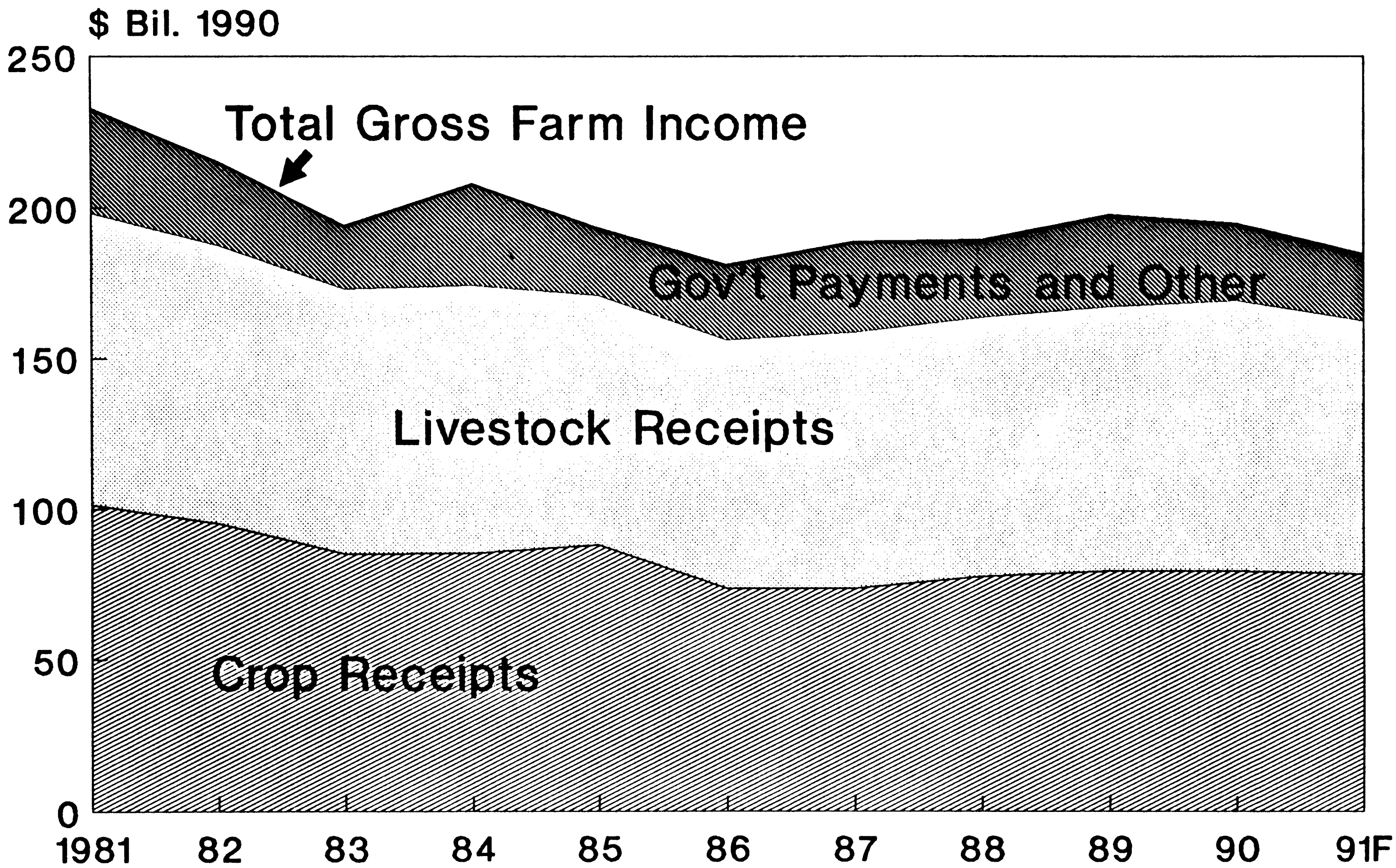
* Direct payments.

* Tariffication.

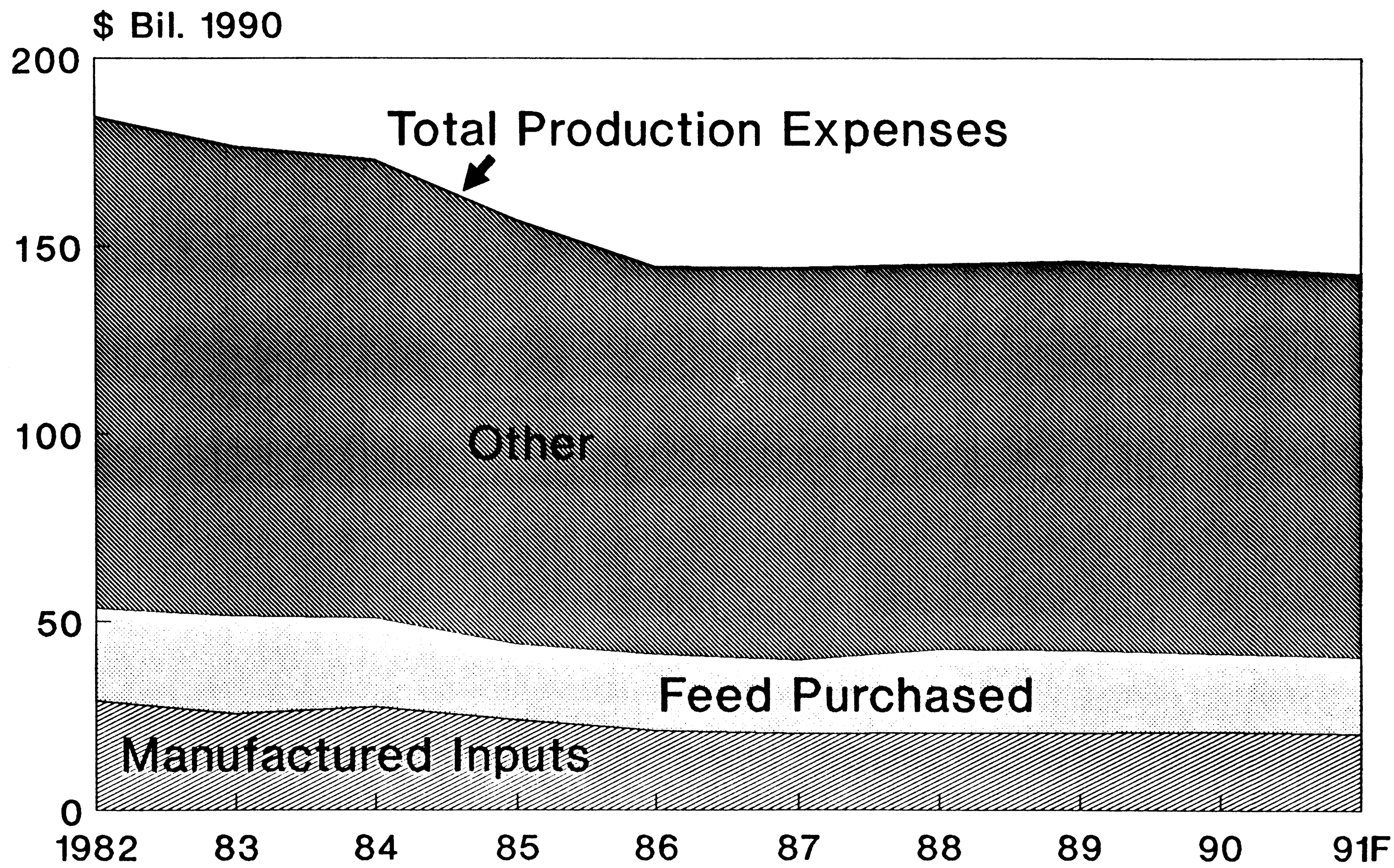
* Production controls.

* Joined with European Free Trade Association.

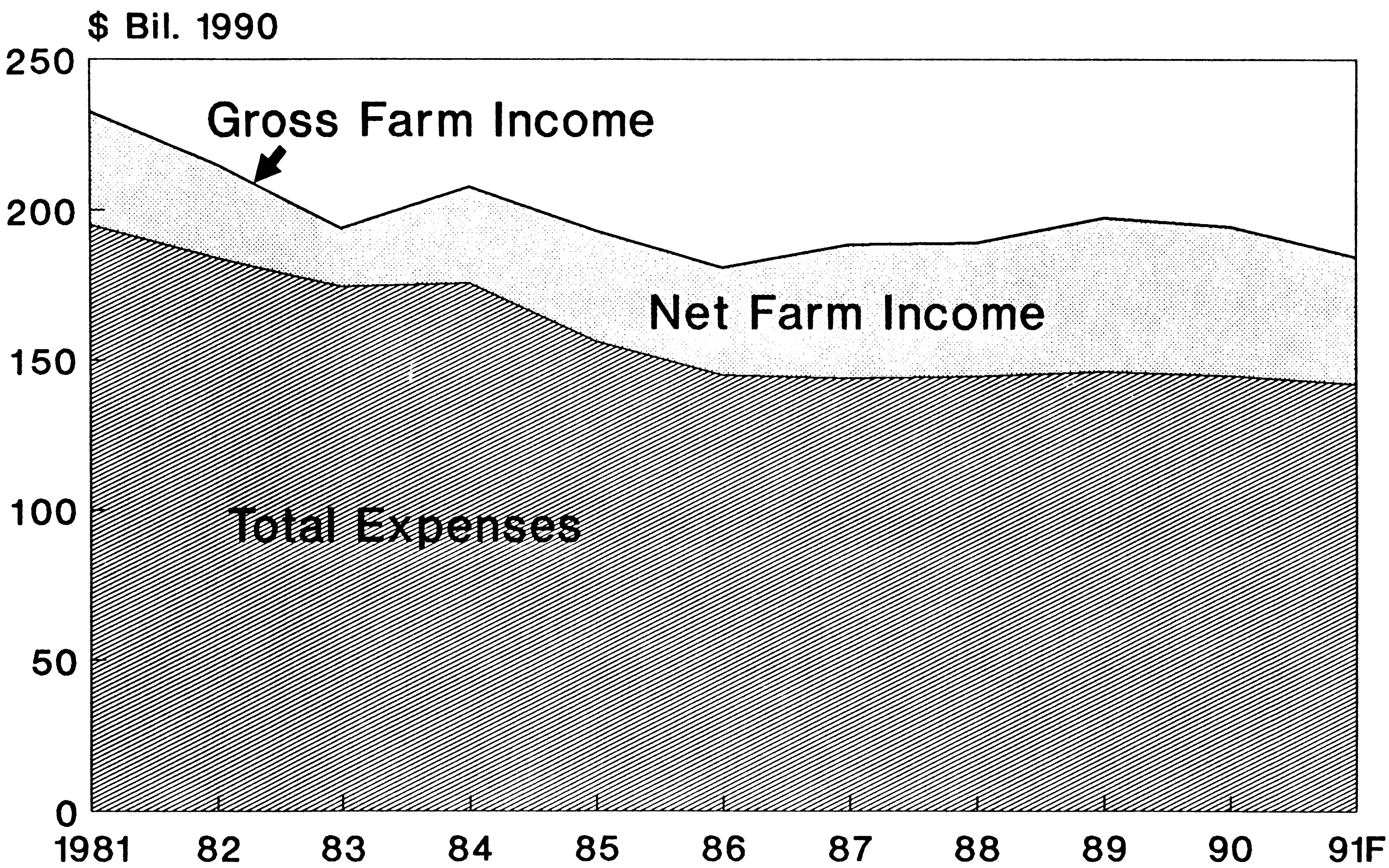
REAL U.S. FARM INCOME AND COMPONENTS



REAL U.S. FARM EXPENSES AND COMPONENTS



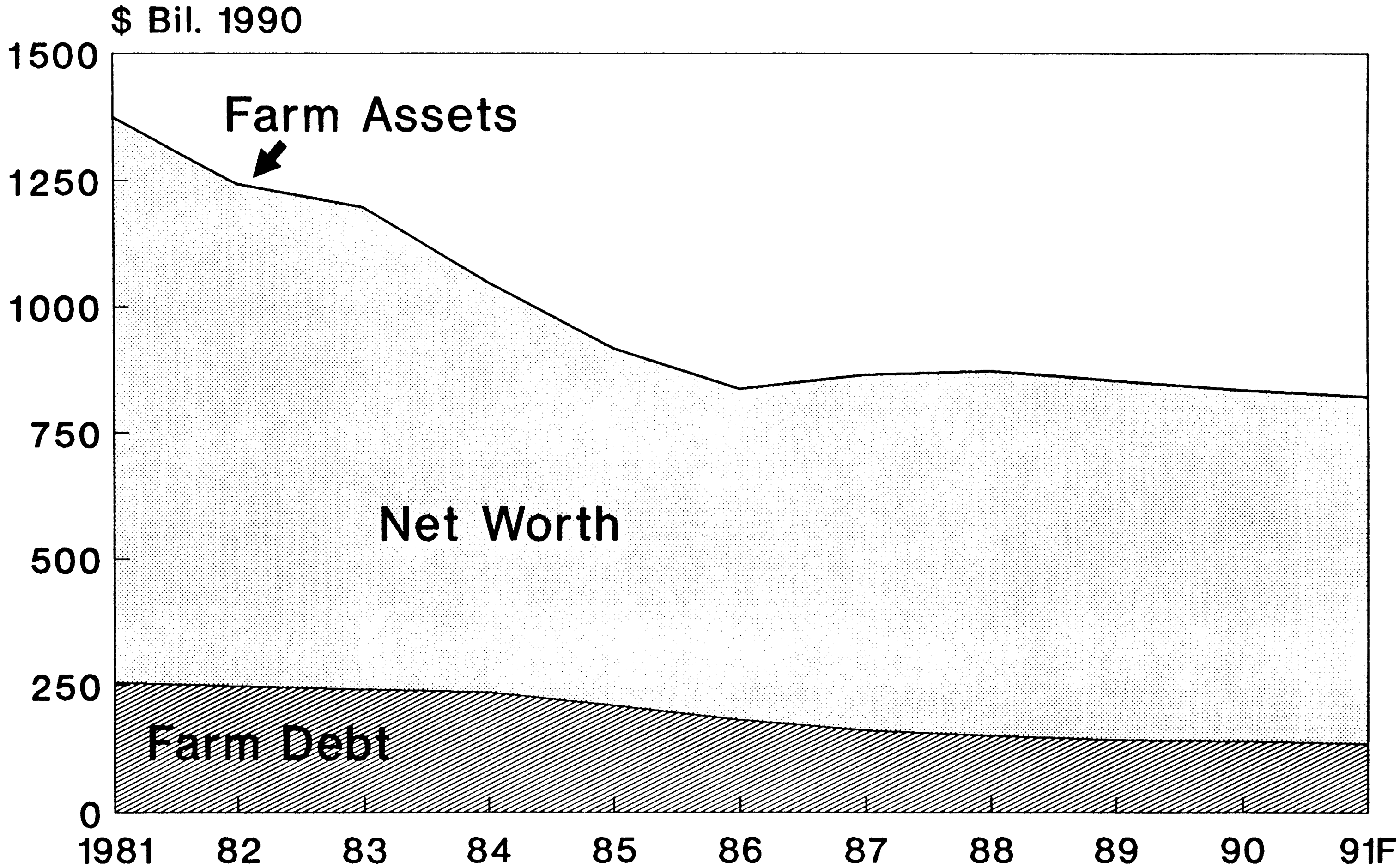
REAL U.S. FARM INCOME AND EXPENSES



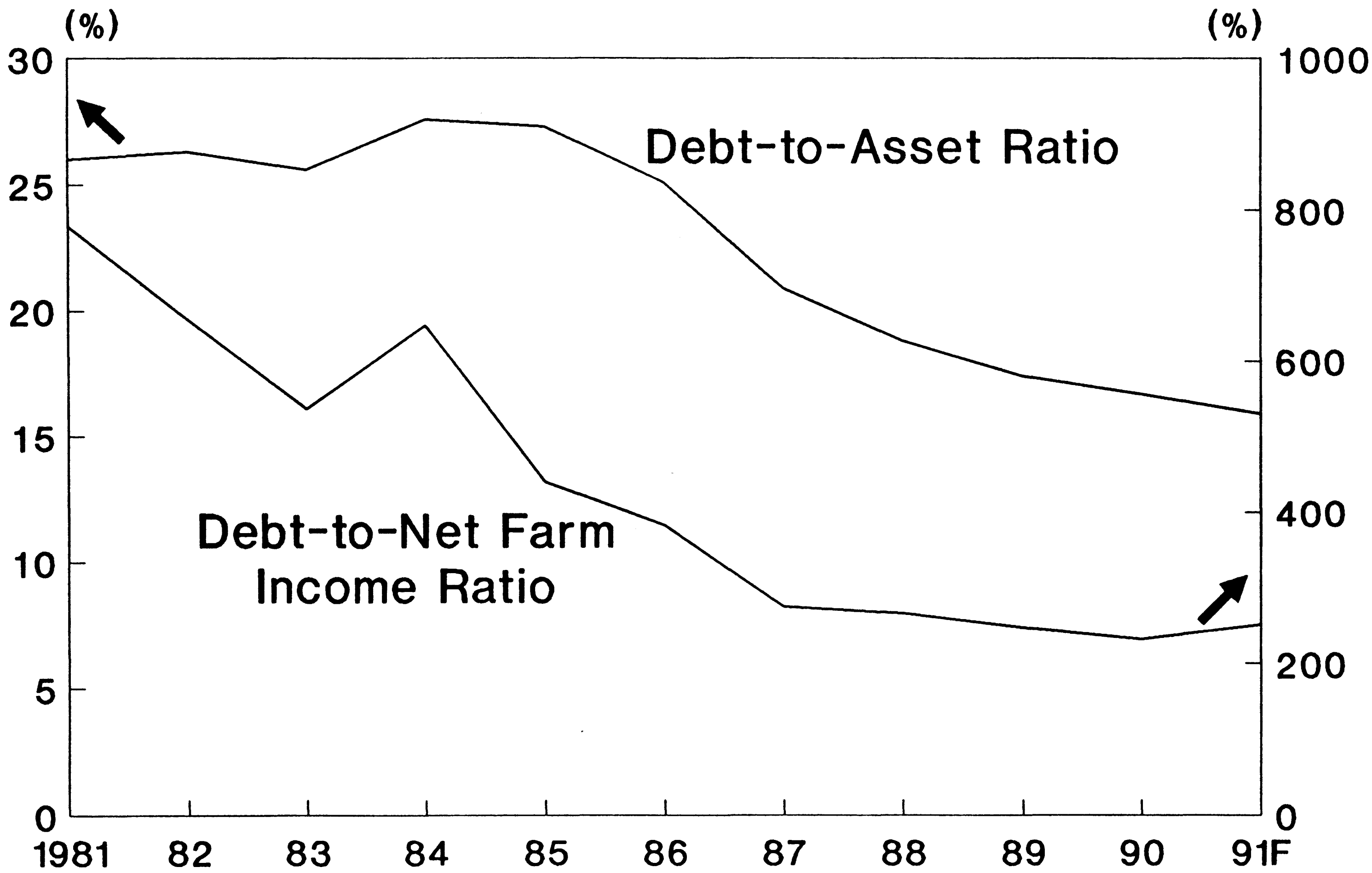
EXPECTED CHANGE IN 1992 OVER 1991, U.S.

	($ Billion)
Crop Receipts	+ 2
Livestock Receipts	0
Total Gross Farm Income	+ 2
Production Expenses	+ 2
Net Farm Income	0

REAL U.S. FARM
ASSETS, DEBT, & NET WORTH



REAL U.S. FARM FINANCIAL RATIOS



MEASURES OF OHIO FARM HOUSEHOLD FINANCIAL CONDITION, 12/31/90

	By Gross Sales		
	Less than $40,000	$40,000-$100,000	$100,000 or More
		($1,000 / farm)	
Assets	356	474	823
Liabilities	26	53	154
Equity	331	421	668
Debt/Assets (%)	7	11	19
Share of farms in:			
- financial stress (D/A > .4)	6	12	18
- severe financial (D/A > .7)	1	2	3